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SUBJECT: Argentina Economic and Financial Weekly for the week ending
June 14, 2006

Weekly Highlights

- Venezuela buys another USD 243 million of Boden 2012 bonds.
- Bolivian and Argentine presidents will announce an agreement on the price of Bolivian gas exports on June 29.
- GOA primary surplus reaches ARP 10.4 billion in the first five months of the year.
- GOA to take over 20 percent of Aerolineas Argentinas stock.
- German Court rules in favor of two bondholders of GOA debt.
- Companies warn that they will not be able to maintain price restraint agreements.
- Commentary of the Week: "Money Doesn't Fix Everything." (Note: We are sending out the Argentine Economic and Financial Weekly early this week due to travel schedules and Argentine Flag Day holiday on Monday, June 19. Our end-of-the-report graphs, which track data on a weekly basis, will resume with our June 23 issue. End Note.)

Venezuela buys another USD 243 million of Boden 2012 bonds.

11. On June 9, the GOA sold USD 243 million of Boden 2012 (a USD-denominated bond maturing in 2012) sold to the Government of Venezuela (GOV). The bonds have a market value of USD 200 million. This is the GOV's sixth purchase this year of GOA bonds, and brings its total 2006 purchases to USD 1.7 billion (at face value, or USD 1.4 billion at market value). In 2005, the GOV purchased USD 1.9 billion of GOA bonds (USD 1.6 billion market value).

Bolivian and Argentine presidents to announce price agreement on Bolivian gas exports on June 29.

12. After more than 6 hours of negotiations, Minister of Planning Julio De Vido returned to Buenos Aires from La Paz with a draft agreement on the price of Bolivian gas exports to Argentina. The presidents of Bolivia and Argentina are scheduled to meet on June 29 to close the final agreement. Although neither country provided details of the draft agreement, the GOA has reportedly agreed to meet Bolivia's offer price of USD 5.5 per million cubic meters. The

GOA had previously counter-offered a price of USD 5 per million cubic meters. In exchange, Bolivia committed to guarantee a gas provision to Argentina of up to 29 million cubic meters a day for the next 20 years. [Argentina currently imports Bolivian gas at a "solidarity" price of USD 3.20 per million cubic meters, while the international price ranges between USD 2.00 and USD 8.00 per million cubic meters.]

GOA primary surplus reaches ARP 10.4 billion in the first five months of the year.

¶3. In a press conference on June 13, Minister of Economy Felisa Miceli announced a primary fiscal surplus of ARP 10.4 billion in the first five months of the year -- compared to ARP 9.9 billion in the same period last year (up 5 percent y-o-y) -- and achieving 53 percent of the ARP 19.4 billion primary surplus target for 2006. In May, the primary fiscal surplus reached ARP 3.9 billion (up 18 percent y-o-y), better than expected, while the overall balance (including interest payments) stood at ARP 3.5 billion. During the press conference, the Minister highlighted that revenues grew at a rate of 17.5 percent, in line with the expenditure growth rate of 17.3 percent, and that the GOA anti-cyclical fund stands at USD 600 million. Private analysts also praised the GOA's fiscal policy of decreasing the growth rate of expenditures and noted that the GOA still will receive BCRA transfers for ARP 550 million, which will boost the GOA primary fiscal surplus in coming months.

GOA to take over 20 percent of Aerolineas Argentinas stock.

¶4. On June 12, Cronista Comercial reported that the GOA and the Spanish group Marsans -- owner of Aerolineas Argentinas (AA) -- are working on an agreement in which the GOA will gain control of more

than 20 percent of AA stock. The agreement is expected to be announced on June 21, when President Kirchner travels to Spain to meet Prime Minister Rodriguez Zapatero. Under the negotiated agreement, the GOA will gain its "golden share" and therefore will hold decision-making power regarding the company's business. According to the report, the GOA will pay for the shares through subsidies to unprofitable AA routes beginning in July.

GOA to announce renegotiation of its Paris Club debt.

¶5. On June 12, Cronista Comercial reported that President Kirchner will formally announce GOA's renegotiation of its USD 6.3 billion Paris Club debt for on June 22 when he meets Spanish Prime Minister Rodriguez Zapatero. However, technical negotiations will not be finished until the end of the year. The GOA envisions a renegotiation in which the GOA recognizes the principal and interest arrears without a principal reduction, but with an extension on maturities at lower interest rates.

German Court rules in favor of two bondholders of GOA debt.

¶6. On June 12, the Frankfurt Regional Supreme Court ruled that the GOA must repay accrued interest and principal on GOA-defaulted bonds worth EUR 5,000 held by two bondholders. The Court said that Argentina has recovered economically and no longer meets the strict requirements to justify a national state of emergency, and therefore it must repay its debt. This ruling may set a precedent for many other cases before German courts, although it will be difficult to enforce given that Argentina has no assets to attach unless the court allows assets held by the Argentine diplomatic offices in Germany to be seized.

Companies warn that they will not be able to maintain price restraint agreements.

¶7. Companies that are members of Copal -- an association of food producers -- are requesting that Secretary of Internal Trade Guillermo Moreno allow them to increase prices due to cost increases. The companies agreed to maintain price levels until the end of June, when they will meet with the GOA to study the option of price increases on a case-by-case basis. . Secretary Moreno met with representatives from major supermarket chains (including Carrefour, Coto, Jumbo, Norte and Wal-Mart) on June 12 to ask for stronger commitments to keep their prices unchanged. Private analysts estimate a CPI increase of 0.7 percent m-o-m for June, following May's increase of only 0.5 percent.

IADB approves USD 40 million credit for Latin America Export Finance Fund.

¶8. On June 8, the Inter-American Development Bank and Crecera Finance Management Company LLC announced a USD 40 million expansion of a trade finance credit facility for Latin America Export Finance Fund (LAEFF). LAEFF is a specialty finance company that provides export finance loan facilities to companies in Argentina, Brazil, Peru and Uruguay. The IADB financing consists of a five-year, USD 10-million loan from its ordinary capital, and of a three-year syndicated commercial bank loan of USD 30 million that may be renewable up to five years.

GOA seeking to regulate private health services fees.

¶9. Superintendent of Health Services Hector Capaccioli stated that the GOA will gain control over private medical health services before the end of 2006, which will allow the GOA to reach price agreements with the sector to avoid rising fees in health care. According to the superintendent, Congress will approve a bill to regulate private healthcare in the second half of 2006. Private healthcare providers recently voiced their demands to raise fees,

which they argue have not been properly adjusted since the 2002 devaluation.

Informal employment decreases 3.2 percentage points to 44.3 percent of employees.

¶10. On June 13, the National Bureau of Statistics (Indec) reported that 44.3 percent of employees (or 4.69 million people) living in urban areas held informal jobs in the first quarter of 2006. According to Indec's survey, informal employment dropped by 80,000 individuals since reaching 47.5 percent of employees (or 4.76 million people) in the first quarter of last year.

Congress to amend the Consumer's Defense Law and increase the powers of the Secretary of Coordination.

¶11. Congress is expected to debate this week an amendment to the Consumer's Defense Law that will increase the powers of Secretary of Internal Trade Guillermo Moreno. Under the amendment, the Secretary will be able to impose fines of up to ARP 5 million on companies that do not comply with consumer defense regulations. Opposition deputies from the PRO party criticized the amendment, arguing that the same secretary will be in charge of arranging price agreements with companies as well as applying fines to those same companies.

BCRA increases passive repo rates by 0.25 percent.

¶12. On June 13, the BCRA announced a 0.25 percent increase in its repo rates, bringing its passive rates to 5.25 percent for one day and to 5.75 percent for seven days (the rates at which the BCRA borrows funds and absorbs liquidity). This is the second increase in passive repo rates this year, and follows a 0.5 percent increase in May. Active repo rates remained unchanged at 7.50 percent this

week, but they also have risen twice this year.

Multilateral real exchange rate depreciates 0.2 percent m-o-m in May.

¶13. The BCRA's multilateral real exchange rate index -- which measures the real exchange rate between the peso and a trade-weighted basket of currencies -- depreciated 0.2 percent m-o-m in May. The real depreciation is mainly mainly the result of depreciation of the currencies of most of Argentina's trading partners (Brazil, Chile, United States and Mexico) against the peso, partially offset by an appreciation of the Euro against the peso, in all cases mainly due to nominal changes and not to a different evolution of price levels in Argentina compared to other countries. The index is 3.5 percent above the level of the last twelve months and 106.9 percent above its average value during convertibility. [The BCRA's multilateral real exchange rate index weighs domestic prices and the exchange rates of Argentina's main trading partners according to their share of Argentina's exports and imports.]

Commentary of the Week: "Money Doesn't Fix Everything.", by Nestor
¶10. Scibona from an article published in La Nacion on June 11

¶14. Perhaps the World Cup will help moderate the electoral climate that has taken over Argentina prematurely, more than a year before the 2007 elections, after Roberto Lavagna erupted into the political scene and became the target of an incipient dirty campaign on the part of ruling party. If that doesn't happen, one will have to pay more attention to the economic numbers than to unproven gossip/accusations and partial truths

¶15. From the political angle, Lavagna has been reproached for having received support from former president Duhalde and his followers, as if Kirchner had not assumed power with the support from the same godfather, nor as if most legislators who previously supported Duhalde had not fled en masse to the lines of the ruling

party less than six months ago. From the economic angle, he has been accused of favoring business clients of the consulting firm that he founded 15 years ago, including some inaccurate accusations (Acindar, for example, clarified that it did not use Ecolatina's services), as if the regimen of tax deductions in question were not driven by the President himself, from whose control no official decision has escaped in the past three years.

¶16. Without being formally in campaign mode, the government has increased public expenditures in the last few months at a higher rate than fiscal revenues have grown, even though tax collections continue breaking records. In the first four months of 2006, against a 22 percent increase in revenues, primary spending driven by the Executive grew almost 36 percent if one excludes transfers to provinces (co-participation) and contributions to the social security system, which are automatic transfers. In the former category, funds set aside for public works grew 91 percent and private sector subsidies 36 percent, according to calculations by the Broda consulting firm.

¶17. In no way does this intensive use of fiscal savings jeopardize the robust total primary surplus, although this year it could fall to 3.2 percent of GDP, compared to 3.4 percent in 2005. Here, the more troublesome data is about the provinces' fiscal situation, which after a surplus of 0.7 percent of GDP last year could close 2006 with a deficit greater than one percent of GDP if they give public employees the 19 percent salary increase set by the federal government. In other words, this means that later on, some provinces, like Buenos Aires could have problems paying December salaries and end-of-the-year bonuses if they do not receive assistance from the federal government.

¶18. If the government believes that continuing to increase spending is the most effective political tool for the coming months, it runs the risk of generating greater inflationary pressures, which it will try to slow down with more price agreements or price controls, as have been used up to now. But this entails another risk, which is

to discourage investment in sectors critical for economic growth.
This can't be fixed with money.

Upcoming agenda

¶19. Argentina has a hefty agenda of pending institutional questions, beyond the macroeconomic soundness that protects it from a crisis. The electoral campaign should really be a debate about solutions for the future, before reviving doubtful focuses on the past. Money cannot fix the fact that the Supreme Court remains incomplete and that the government is avoiding a decision on whether it will fill the two vacancies that prevent the Court from ruling on questions of law/constitutionality or if it will reduce its composition to seven members.

¶20. Nor can it fix that the executive branch is renegotiating public service concessions in the energy sector, or that it is washing its hands of their fulfillment. Nor that the University of Buenos Aires continues to be leaderless after nearly two months due to the use of force, without anyone being held responsible for it.

¶21. More public funding cannot resolve a problem that was quantified by the National Institute of Statistics and Census (INDEC): two out of every ten businesses cannot fill vacancies, because they cannot find qualified personnel in distinct industrial and service sectors. The reform underway in the education law should concentrate on adapting its content to the real necessities of the country; but it will be difficult if one does not value the culture of knowledge and if one makes businesses the enemies of society.

¶22. For the umpteenth time, Congress postponed mortgage foreclosures for 180 days, but it has not provided an in-depth solution that allows for a normalization of relations between debtors and creditors the reactivation of credit for housing for middle and lower-income sectors. This isn't unusual, because Congress has delegated broad powers to the executive branch, including the power to apply discretionary tariff charges to finance energy works that do not figure into any known plan. ...

¶23. None of these problems, nor many others, can be fixed with money. They don't have the sex appeal of wars of provocation, nor the attraction and distraction of goals scored by the national soccer team. But it is time, for once, to go beyond discussing the rigid divisions of being in favor or against, even if it's no more than to restore the image of Argentine leadership in the face of a new wave of political cannibalism. (Note: We reproduce selected articles by local experts for the benefit of our readers. The opinions expressed are those of the authors, not of the Embassy. End Note.)

GUTIERREZ